

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)	
)	
Modifying the Commission's Process to Avert)	IB Docket No. 05-254
Harm to U.S. Competition and U.S. Customers)	
Caused By Anticompetitive Conduct)	

COMMENTS OF MCI, INC.

Sasha Field
MCI, Inc.
1133 19th Street, NW
Washington, DC 20036
(202) 736-6034

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MCI, Inc. ("MCI") submits these comments in response to the Commission's Notice of Inquiry ("NOI") in the above-referenced proceeding.¹

I. INTRODUCTION AND SUMMARY

MCI applauds the Commission's timely decision to undertake this NOI in an effort to determine whether the FCC should adapt its policies and procedures regarding "whipsawing" to ensure that they remain effective and efficient in light of changes in the marketplace. One of the Commission's core missions is to ensure that rates paid by customers in the United States are just and reasonable.² The Commission has a wide array of tools at its disposal to address anticompetitive behavior that harms U.S. customers and broad authority to ensure that the public interest is not harmed by anticompetitive actions by market participants, whether foreign or domestic.

¹ *Modifying the Commission's Process to Avert Harm to U.S. Competition and U.S. Customers Caused By Anticompetitive Conduct*, IB Docket No. 05-254, Notice of Inquiry, FCC 05-152 (rel. Aug. 15, 2005) ("NOI").

² 47 U.S.C. § 201(b); *International Settlements Policy Reform, International Settlement Rates*, First Report and Order, 19 FCC Rcd 5709, ¶ 41 (2004) ("ISP R&O"). *See also, id.* at ¶ 91.

Over the years, the Commission has developed many specific policies and procedures aimed at addressing anticompetitive behavior by market participants on international routes. However, the past few years have seen rapid evolution in the international telecommunications market, both in terms of technology and the competitive landscape. For example, the U.S. end of U.S.-international routes has become increasingly competitive, while carriers on the foreign end of many routes continue to enjoy market power. It is the abuse of this market power that often leads to the unilateral imposition of unjust and unreasonable rates, terms or conditions on U.S. carriers.

As the Commission has recognized, it must play a central role in protecting U.S. carriers and customers from those abuses. Specifically, the Commission must take swift and effective action to prevent and/or undo anticompetitive circuit disruptions or other attempts at whipsawing. The Commission must be careful, however, to tailor its actions to suit the current competitive landscape. Some of the Commission's traditional remedies may prove less effective today given changes in the marketplace and in technology.³ Therefore, it is critical that the Commission use this NOI to educate itself on the changes in the marketplace and open a proceeding to propose changes designed to improve the FCC's ability to respond swiftly and effectively to threats of whipsawing.

II. DISCUSSION

A. The Commission Has Both the Authority and the Responsibility to Address Whipsawing

As a threshold matter, the Commission has jurisdiction to address issues related to inappropriate circuit disruption and other anticompetitive behavior on the part of foreign carriers.

³ For example, carriers may be able to circumvent stop-payment orders by re-routing traffic via indirect means and suppressing Calling Line Identification, thereby disguising the country of origin.

In the *ISP Reform Order*, the Commission reemphasized its position that it has “broad authority to protect U.S. consumers from harms resulting from anti-competitive behavior.”⁴ The FCC has taken a two-pronged approach to protecting U.S. customers, exercising its jurisdiction over U.S. carriers to combat abuses of market power by foreign carriers, while also working with international bodies and foreign regulators to promote competition. For example, the Commission has used its authority over U.S. carriers to adopt benchmark policies, issue stop-payment orders, enforce dominant carrier provisions, and take other similar actions to protect U.S. carriers and customers from anticompetitive behavior by foreign carriers. Such regulatory action has been upheld by the courts – including the U.S. Court of Appeals for the District of Columbia, which noted that “the Commission does not exceed its authority simply because a regulatory action has extraterritorial consequences.”⁵ The Commission has also been active in the international arena, taking strong pro-competitive positions in international fora such as the International Telecommunication Union and World Trade Organization, and working with foreign national regulatory authorities (“NRAs”) to support and encourage independent, transparent, and pro-competitive regulatory environments in other countries.⁶

Consistent with the Commission’s deregulatory goals, the FCC should continue to allow the market to work and permit carriers to negotiate their own agreements whenever possible. However, the Commission must also continue to recognize that there are some instances in which carriers on the foreign end of a U.S.-international route have market power and can use

⁴ ISP R&O, ¶ 91.

⁵ *Cable & Wireless P.L.C. v. FCC*, 166 F.3d 1224, 1230 (D.C. Cir. 1999).

⁶ These activities are critically important, as foreign regulators are more likely to be receptive to overtures from the FCC than to arguments by individual U.S. carriers. In MCI’s experience, some foreign regulators are quick to dismiss or ignore facts presented by MCI, instead offering blind support to foreign carriers that are whipsawing MCI and other U.S. carriers.

that market power to extract harmful concessions from U.S. carriers. In those situations where the market fails, the FCC must use the full extent of its legal authority to prevent or rectify anticompetitive actions and protect the public interest.

B. Anticompetitive Circuit Disruption is Outside the Scope of Reasonable Commercial Behavior and Reflects an Abuse of Market Power

The Commission has found that U.S.-international carriers “face robust competition”⁷ and that this competition continues to intensify.⁸ There are almost sixty U.S. facilities-based and facilities-resale carriers and more than 750 resale providers licensed to carry traffic into and out of the United States.⁹ Moreover, network technology has now developed to a point where it is easier than ever to reroute traffic or increase capacity, thus allowing carriers to take advantage of market shifts, even on routes on which they have not played a significant role historically. Intense competition, coupled with dramatic increases in circuit capacity and decreases in costs-per-circuit,¹⁰ have resulted in significant declines in revenues-per-minute even as billed minutes have grown dramatically.¹¹ Rates for calls to a wide range of countries and regions have fallen

⁷ ISP R&O, ¶ 73.

⁸ *Id.*, ¶ 2.

⁹ In 2003, 845 carriers filed international telecommunications data report pursuant to Section 43.61 of the Commission's rules, of which 57 were U.S. facilities-based and facilities-resale carriers and 770 were pure resale providers. (The remaining 18 carriers requested confidential treatment.) Federal Communications Commission, International Bureau, 2003 *International Telecommunications Data (Filed as of October 31, 2004)*, at 1 (Jan. 2005), available at: <http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/Intl/crepor03.pdf>.

¹⁰ See Federal Communications Commission, International Bureau, *Trends in the International Telecommunications Industry*, at 9-10 (Sept. 2005), available at: <<http://www.fcc.gov/ib/sand/mniab/traffic/files/ITRND01.pdf>> (“*Trends Report*”).

¹¹ *Trends Report* at 6; *id.* at Figure 6 (average revenue per minute declined over 84% between 1980 and 2003, while U.S. billed minutes increased from 1.6 billion to 42.7 billion over that same period); see also *Wireline Competition Bureau Federal Communications Commission Biennial Regulatory Review 2004*, Staff Report, 20 FCC Rcd 263, ¶ 7 (2005).

significantly in recent years.¹² These benefits may be undermined, however, if foreign carriers are able to abuse their market power on the foreign end of an international route to force concessions that they could not otherwise gain from U.S. carriers through commercial negotiations.

As the Commission stated in the NOI, it has “recognized that anticompetitive conduct that disrupts normal commercial negotiations for the purpose of forcing U.S. carriers to accept above-cost settlement rate increases harms the public interest.”¹³ Any refusal to terminate traffic (or other variant on blocking) that is designed to force a change in rates or other terms or conditions in a manner that is inconsistent with the terms of the parties’ commercial agreements harms the public interest and requires immediate action by the Commission. In addition to leading to higher rates for U.S. customers, “whipsawing” has the more insidious effect of undermining the workings of a competitive market by devaluing the worth of commercial agreements.¹⁴

C. Anticompetitive Circuit Disruption Harms U.S. Customers

By their very nature, anticompetitive circuit disruptions harm U.S. customers. The harm is not simply that rates may increase, or terms or conditions may become less favorable. Indeed, even in a free and competitive market it is possible for rates to increase (when, for example, there is an increase the underlying costs of providing service) or for carriers to accept less favorable terms or conditions as market conditions change. The true harm from whipsawing is to the integrity of the negotiating process.

¹² See *Trends Report* at 6.

¹³ NOI, ¶ 1.

¹⁴ The Commission noted the benefits of commercial agreements and individually-negotiated contracts and termination rates in discussing the benefits of lifting the ISP. See, e.g., ISP R&O, ¶ 28.

In a free market, carriers should be able to negotiate the best possible rates, terms and conditions. Some carriers may be able to differentiate themselves from other carriers based on their superior negotiating skills or business acumen. Carriers in a competitive market may also make trade-offs, conceding one point in a negotiation in order to achieve a more favorable result on another issue. This give-and-take is the natural result of a free and competitive market. If foreign carriers are able to use their market power on the foreign end of a route to extract concessions and essentially remake those parts of the negotiated contract that no longer appeal to them, it makes a sham of the entire negotiating process and undermines the integrity of the market.¹⁵

Nonetheless, it is important to remember that carriers do not act in a vacuum and that their actions may have significant consequences for their customers. Unilateral action by foreign carriers can have drastic harmful effects on U.S. end-users. Take, for example, a representative Latin American route, such as the U.S.-Bolivia route. Using data from the Commission's 2003 43.61 report, MCI has calculated that there are an average of 27,872 messages per day on this route.¹⁶ This means that more than 25,000 customers would likely be affected if circuits were blocked for even twenty-four hours. Using rough estimates based on MCI's own data for 2005 suggests that one day of blocking on the U.S.-Bolivia route would have harmed an average of

¹⁵ MCI does not expect the FCC to intervene in those rare situations where circuit blockages or other disruptions harmful to a U.S. carrier occur consistent with the terms of a freely-negotiated contract. The Commission should act only where the disruption or blockage is the product of a foreign carrier's attempt to abuse its market power to coerce concessions from U.S. carriers. In those cases where a foreign carrier is acting pursuant to rights it obtained through a free and fair negotiation and is not abusing its market power, the FCC should not interfere with the commercial relationship and should allow the parties to achieve a negotiated resolution of the problem.

¹⁶ MCI based its calculations based on a twenty-four hour period under the assumption that it may take as little as twenty four hours in a situation where all U.S. carrier circuits are blocked for other carriers to open up sufficient capacity to either carry the traffic on behalf of the blocked carriers or to lure away customers and carry their traffic directly.

more than 14,000 MCI customers. Blocking on routes with higher traffic volumes, of which there are many, would affect even more customers.

D. The Commission Should Focus on Abuses of Market Power Designed to Override Negotiated Commercial Agreements

In the NOI, the Commission asks how it should define circuit disruptions or blockages.¹⁷ In contrast to the intense competition that exists among U.S. carriers seeking to originate international calls, foreign carriers often have market power which they can use as leverage to achieve changes in rates or other terms or conditions that they may not be able to obtain through direct negotiations. Worse, this abuse of market power is sometimes supported or even encouraged by the foreign government. Thus, at its simplest, inappropriate circuit disruption should be seen as any use of market power to act outside of the scope of a commercial relationship for the purpose of forcing another party to change commercial terms.¹⁸

Thus, in MCI's view, the FCC should not focus only on blockages that prevent termination of all traffic on a route. Rather, the Commission should focus more broadly on the range of possible ways in which a carrier can use its market power to act in a manner that is not commercially reasonable. For example, the Commission should be concerned if a foreign carrier refuses to terminate certain subsets of traffic – such as mobile traffic – unless U.S. carriers agree to pay higher rates for that traffic. The Commission also should be concerned about actions that degrade the quality of service being provided – for example, by degrading the quality of service requirements of ADSL lines in such a way that VoIP traffic cannot be transmitted.

¹⁷ NOI, ¶ 8.

¹⁸ It is conceivable that in certain circumstances a carrier or carriers could act in a manner that is technically within the scope of the commercial relationship but would nevertheless constitute an abuse of market power that requires the Commission's attention.

Anticompetitive behavior could also consist of “choking” traffic so that only a portion of the traffic is actually terminated on the foreign end.

However, the FCC should allow for circumstances where it is appropriate for a carrier to refuse or limit traffic termination. For example, where there is a genuine technical problem – such as where the inbound traffic is truly harming or overwhelming the network – a carrier may have a legitimate need to refrain from terminating traffic from another carrier. In addition, there are situations where a carrier is within its contractual rights to refuse to terminate traffic from another carrier. Neither of those situations should require FCC action.

E. The Commission Should Act Immediately to Thwart Threats of Anticompetitive Blockages

As the Commission recognized in the NOI, threats of circuit disruptions or blockages create “exigent circumstances” that demand swift action from the FCC in order to protect U.S. competition and customers.¹⁹ In particular, the Commission must be able to act expeditiously to prevent foreign carriers from “whipsawing” U.S. carriers into accepting unfair terms and conditions that harm U.S. customers.²⁰ Shortening the comment cycle, as AT&T suggested,²¹ would likely provide at least some benefit by expediting the Commission’s ability to resolve complaints or petitions alleging whipsawing.

A shortened comment cycle alone is not enough, however. The Commission also should adopt procedures for taking interim measures upon notice that foreign carriers have threatened U.S. carriers with circuit disruptions or otherwise tried to “whipsaw” U.S. carriers into accepting

¹⁹ NOI, ¶ 9.

²⁰ As the Commission noted, once one carrier accepts the terms and conditions of a whipsawing foreign carrier, other U.S. carriers are likely to follow. *Id.*, ¶ 9.

²¹ *Id.*, ¶ 9.

terms and conditions that are harmful to U.S. consumers and U.S. carriers.²² The Commission's rules already provide that "[i]n the event significant, immediate harm to the public interest is likely to occur that cannot be addressed through *post facto* remedies, the International Bureau may impose temporary requirements on carriers authorized pursuant to § 63.18 of this chapter without prejudice to its findings on such petitions."²³ To date, however, the Commission has not established the procedures pursuant to which it will exercise this interim authority.

There are numerous ways in which the FCC could exercise its authority to take interim measures. The simplest possibility would be for the Commission to issue a Notice of Proposed Rulemaking seeking comment on the types of actions that should be considered to be presumptively anticompetitive and that are likely to result in immediate harm that cannot be addressed through *post facto* remedies.²⁴ After notice and comment, the Commission would then issue an order delineating the activities, or class of activities that would be considered presumptively unlawful and result in immediate interim action by the FCC.²⁵ The order would place all carriers on notice that the FCC may take immediate action if it has credible evidence of whipsawing.²⁶ Thereafter, the FCC would impose immediate interim relief whenever it found

²² See *id.*, ¶¶ 9-10.

²³ 47 C.F.R. § 64.1002(d).

²⁴ These presumptively unlawful activities might include, for example, circuit disruptions, blockages or degradation, or threats of any such actions.

²⁵ Interim measures might include, for example, orders prohibiting U.S. carriers from making payments to the offending foreign carrier(s) or freezing the *status quo* (i.e., maintaining current terms and conditions) until the whipsawing concerns can be resolved and the Commission is confident that U.S. carriers will be able to negotiate fair terms and conditions with the foreign carrier(s).

²⁶ This evidence may consist of reports by one or more U.S. carriers, copies of written notifications of proposed actions by foreign carriers, or any other information that the FCC finds to be credible. It is unrealistic to expect that U.S. carriers will always have written evidence of a foreign carrier's threat to block circuits. Where such "smoking guns" are not available, the FCC may rely on one or more reports of threats. For example, if multiple U.S. carriers independently

credible evidence that a foreign carrier had taken, or was threatening to take, actions that the FCC had identified as being presumptively unlawful.

Any relief imposed by the Commission pursuant to these procedures would be temporary and would not prejudice the ability of a foreign carrier to demonstrate that its actions were reasonable.²⁷ If a carrier were able to overcome the presumption of unreasonable conduct, the FCC would lift the interim relief and allow U.S. carriers to negotiate freely with the foreign carrier(s).²⁸ If the foreign carrier were unable to overcome the presumption of unreasonableness during a proceeding that allows for comments and reply comments, the FCC could impose additional relief or make permanent its grant of temporary relief.

F. The FCC Should Tailor Its Remedies to Maximize Their Effectiveness

The Commission has a broad array of remedies at its disposal to address whipsawing. The Commission has jurisdiction over any carrier that holds a Section 214 authorization or other licenses or authorizations granted by the Commission. The Commission may exercise this jurisdiction in a number of ways.

notify the Commission that a particular foreign carrier has threatened to block circuits unless certain conditions are met, the FCC should view the corroborated, independent reports as credible evidence that the foreign carrier has threatened to engage in whipsawing. In order to encourage carriers to report concerns to the FCC, the identity of carriers reporting such behavior should be treated as confidential, at least until the FCC initiates a proceeding to examine the complaints. Otherwise, fear of retaliation by foreign carriers may inhibit U.S. carriers' willingness to report threats of whipsawing.

²⁷ Foreign carriers' attempts to rebut the Commission's presumptions and have the interim relief rescinded should be subject to an expedited pleading cycle, similar to whatever expedited schedule the Commission adopts for resolving petitions or complaints regarding whipsawing.

²⁸ The Commission could also allow "true-ups" or take other actions necessary to restore the foreign carrier to the position it would have been in had the Commission not imposed interim relief based on a presumption that was later rebutted.

1. Market and Technological Development Require a Thorough Economic Analysis

Any action the Commission takes must address the manner in which the “market” reacts to attempts to exercise market power. The reaction in the market exemplifies the very different circumstances that exist today from the not too distant past. As discussed above, there has been an explosion in the number of carriers serving international routes over the past decade, and intertwined with this expansion has been the accompanying evolution of network technology to allow for smoother, faster, more flexible interconnection, routing, capacity and quality of transmission.

Carriers are significantly more interconnected than in the past. To efficiently manage their own network capacity, facilities-based carriers such as MCI are interconnected with multiple resellers. These interconnections permit the use of resellers’ capacity when appropriate – for example, to handle peak loads along a given route when construction of additional direct capacity would not be cost-effective. These interconnections also allow facilities-based carriers to respond rapidly if traffic conditions change significantly in a short time. The existence of such an intricate web of interconnections between facilities-based carriers and resellers is a key distinction from technical conditions in the past, and should not be ignored.²⁹

This greater degree of interconnectedness and the number of carriers in the market(s) are key to understanding the evolved and complex conditions that exist today. In addition, these conditions provide the means to understand the disparate incentives that exist among carriers – incentives that must be taken into account to achieve a sound policy result.

²⁹ It is no coincidence that the explosion in the number of resellers has occurred during the same period in which transmission costs have fallen dramatically. Thus, managing the exchange of international traffic between a facilities-based carrier and its reseller vendors mandates that ample capacity be available. To skimp on interconnected capacity would be a “penny wise, pound foolish” proposition.

More specifically, assume that a foreign carrier demands higher termination rates from all carriers serving a given route. Further assume that it is likely that the foreign carrier will block or disrupt traffic from any carrier who does not readily accept the higher rate. Under these conditions, at least two very different incentives may drive the carriers' reaction. On the one hand, some carriers may be concerned about the impact of higher rates on their customers and their cost basis and thus be reticent to accept the higher rate. The incentive for these carriers is to work through their commercial relationship to come to a negotiated solution that they could support. Conversely, some carriers may see a competitive opportunity in any such hesitation by other carriers. The incentive for these carriers would be to increase share along the route (at the expense of other carriers).

If the foreign carrier acts on its threat to block or disrupt traffic from carriers that do not agree to pay the higher termination rate, those carriers face the prospect of customer disruption. To protect their customers, carriers must arrange alternatives to direct terminations with the foreign carrier. It is these alternatives that permit other carriers to gain market share on the route.

Accomplishing such a market share gain is not at all difficult from a technical standpoint. Global networks are interconnected to such a degree that indirect routing presents few, if any, technical barriers. Further, the masking of identifying information on calls means that traffic that can no longer be terminated directly over a given route is readily terminated indirectly without knowledge by the foreign carrier. It is the fact that customer traffic can ultimately reach the intended destination – whether via direct or indirect means – that creates the incentive for certain carriers quickly to accept higher rates without regard for the ultimate impact on consumers.

Thus, the interconnectedness of global networks and the numerous carriers who are able to handle additional traffic creates something akin to a “first mover advantage” in reacting to proposed termination rate increases by foreign carriers, notwithstanding that such behavior ultimately leads to higher cost commitments and increased rates for consumers. Any true assessment of possible actions requires that the Commission first assess of the complex economics surrounding such multi-level market behavior.

2. Comments on Specific Remedies

Although it is difficult to address specific remedies before addressing the current nature of the market more thoroughly, there are nevertheless certain comments MCI can make at this point. One remedy employed by the Commission in the past has been stop-payment orders, prohibiting U.S. carriers from paying foreign carriers until they cease to engage in anticompetitive behavior. The effectiveness of stop payment orders may be limited, however, to the extent that foreign carriers can re-route traffic and/or expand their capacity loads so that they can pick up the lost traffic either directly from U.S. carriers, or indirectly by luring away customers.

A more effective solution may be to prohibit all U.S. carriers and cable landing license holders from carrying or terminating traffic from foreign carriers that are engaged in whipsawing, or have threatened to do so. Another alternative would be for the Commission to order all U.S. carriers to implement unilateral rate increases for traffic between the United States and any country in which carriers are engaging in circuit blocking or other anticompetitive activities. This would raise the foreign carrier’s costs, thereby creating a disincentive to counter the perceived benefits of blocking. This would put pressure on the foreign carrier(s) to retreat from their threats of (or actual) blockages and help level the playing field by allowing U.S.

carriers (which are subject to competition and therefore lack market power) to retaliate effectively against attempts by foreign carriers to abuse their market power.

This NOI is not the proper vehicle for reaching final decisions about potential remedies, however. Before the Commission adopts specific remedies, it should gather information about the market and determine which remedies will be most effective in addressing specific anticompetitive situations. This is particularly important given the risk that certain “remedies” may in fact prove counter-productive or even harmful to U.S. carriers and customers.³⁰ This NOI provides an excellent forum for beginning to understand the various problems U.S. carriers face in dealing with foreign carriers with market power and laying out the expansive range of remedies available to the Commission (some of which are discussed above). However, the Commission should launch an inquiry or further proceeding to probe the technical and competitive aspects of the market in greater depth before adopting any specific remedies or procedures.

G. The Allegations of Failure to Pass Rate Decreases Through to End Users are Irrelevant and Disingenuous

In the NOI, the Commission noted that some foreign government officials have alleged that U.S. carriers fail to pass the benefits of lower termination rates through to their customers.³¹ From MCI’s perspective, this simply is not the case. The portion of the international telecommunications market in which MCI participates is so competitive that carriers cannot price services significantly above their marginal costs without losing large numbers of customers to competing providers. This is particularly true in the international wholesale market, where

³⁰ See, e.g., ISP R&O, ¶ 47 (explaining that re-imposing the ISP’s requirements may not effectively address a particular anticompetitive harm and may cause further detriment to U.S. competition and U.S. customers on a route).

³¹ NOI, ¶ 12.

margins are razor thin – often barely covering the integrated cost of service provided – and where MCI is increasingly active.³² Indeed, as the Commission recently concluded, “average price reductions [have] substantially outpaced settlement rate reductions . . . reflecting pass-through of settlement rate reductions as well as other cost savings and increasing competition in the U.S.-international market.”³³ As the Commission has explained, “because U.S.-international telecommunications carriers face robust competition in most markets, it is not surprising that changes in settlement rates have been passed on to end-users in the United States.”³⁴

³² As a result of the shifting nature of the customer base – from primarily single consumer to primarily wholesale and large business customers (who often are able to negotiate steep discounts in rates) – the Commission and foreign regulators should be wary of relying on the rates posted publicly on carriers’ websites or reported pursuant to the Commission’s reporting requirements to determine whether savings are being passed through to customers. Neither of those sources accurately reflects the current prices paid by the majority of major carrier customers on most routes.

³³ ISP R&O, ¶ 72; *see also id.* n.179 (noting that calling rate reductions exceeded reductions in net settlement rates by an even greater amount than they exceeded reductions in settlement rates).

³⁴ ISP R&O, ¶ 73.

III. CONCLUSION

For the reasons set forth above, the FCC should act promptly to protect U.S. customers and U.S. carriers from the harms caused by the abuse of market power exercised when foreign carriers engage in harmful and anticompetitive circuit disruption.

Respectfully submitted,

/s/Sasha Field
Sasha Field
MCI, Inc.
1133 19th Street, NW
Washington, DC 20036
(202) 736-6034

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